

Tools of Wealth Newsletter



What Happens In Nevada Probably Shouldn't

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By Lee R. Phillips, JD

Any time you are conducting some sort of a business activity or owning rental real estate, you should be seriously considering the use of a "company" to limit your liability. State statutes govern the structuring of various companies that will limit your liability. Such "companies" include corporations, limited liability companies (LLCs), and limited partnerships. In order to encourage entrepreneurs to take the risks of conducting business or dealing with tenants, laws have been adopted that allow the entrepreneurs to create a company and get personal liability protection. The laws are really quite uniform from state to state, because lawyers have gotten together and created "uniform" acts (laws) that have been adopted by each state.

Even though the uniform acts have been adopted by all states, the laws aren't exactly uniform from state to state. Some states have only adopted certain portions of the

acts or have "changed" parts of the acts to meet the whims of the state's law makers. The courts in some states have made "funny" rulings that strengthen or weaken the laws passed by the legislators. Thus, there is always the question, "Which state should I form my company in?" I will try to answer that question in this article.

For purposes of this article I will talk about corporations rather than Limited Liability Companies. However, you will want to use an LLC in 90% of your business structures, because the LLC not only gives you the "corporate shield," it also gives you charging order protection. LLCs are usually simpler to create and maintain than corporations. You can think of LLC "rules" as a subset of the corporate "rules." So if we consider a corporate structure in this article, it will certainly



allow you to structure and maintain an LLC. You should note that the "subset" of rules that apply to an LLC is different from LLC to LLC, because the rules that have to be followed depend upon how the papers are written that create and operate the LLC. Some of the rules are required by law, but many of them are imposed on the company (corporation or LLC) by what you adopt as your by-laws (operating agreement for LLCs).

Delaware is the king of corporate law. They started years ago trying to attract corporations to their state, and they did a good job. Almost every company that is publically traded in any form is home based in Delaware. By far more cases involving corporations (and LLCs) are tried in Delaware than any other state. Delaware is almost always the first to come out with new and improved laws. Other states saw what Delaware did and they got on the bandwagon. Nevada has been particularly aggressive in marketing its corporate structures to everyone and their dog, and there are now a ton of Nevada corporations. Wyoming and Colorado are riding the bandwagon along with almost every other state, except California and possibly New York, which do everything they can to discourage business.

With all the hype being thrown at you, which state do you form your company in? In almost every case, you should form your company in the state where its assets are held or where it is "doing business." You might note that a company has to be registered (filed) in every state where it is "doing business." The law has a funny idea of what "doing business" means. If the company owns property, contracts, signs leases, hires an employee, or does any one of ten dozen other things, it is doing business and must register in the

state. If you do business in Ohio and incorporate in Nevada, you will be required to register in both states. When you were sold your Nevada corporation, the sales dudes forgot to stress that point. (I am going to beat up Nevada corporations pretty big time in this article, so don't get your feelings hurt if you have a Nevada corporation. You are in good company with many others.)

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Registration in a state requires you to pay all of the corporate fees, appoint a registered agent to receive legal papers (process) for you, and file taxes in the state. Of course, if you are incorporated in another state (Nevada for example) you will have to register in that state, get your registered agent, and do the tax stuff. Depending upon the state, there may or may not actually be an income tax owing. Nevada actually has a state corporate tax in some situations, and in the past couple of weeks they have imposed two new annual fees that add an additional \$350 per year to your bill if you have an LLC. The annual fees vary dramatically. For example, it costs \$70 in Utah and \$800+ in California. If you are incorporating in Nevada or Delaware and you don't live there or have some warm body to act as your registered agent, you will have to hire a registered agent. That runs anywhere from a couple of hundred dollars a year to a couple of thousand dollars a year.

Any way you cut it, it will be a lot more expensive to have a corporation in a state where you are not actually doing business. So why do it? Nevada will tell you that your identity will be "secret." They have "absolute secrecy." Yeah sure, and I am Santa Claus. The courts in any state can compel testimony of the Nevada agents and disclosure of the principals of any corporation. Do you really think your registered agent or attorney in Nevada is going to go to jail for contempt of court to protect your identity? Yes, discovering the owners of the company is one more argument an attorney will have to make when your corporation gets sued, but it isn't a hard argument to make. Everyone already knows who "owns" the company. You have already had to sign personally on all your accounts and mortgages. Your creditors, tenants and everyone else knows you own the company, so discovering your true ownership is just a formality.

Oh, you have been told by your Nevada corporate sales dude that Nevada doesn't have any information-sharing agreement with the IRS. If you have been following the papers recently, you have noted that Switzerland has just handed over all of its banking records to the IRS. Any country in the world that won't share its banking records with the IRS is considered an enemy of the state. I don't recall the US sending troops to Las Vegas lately. And trust me, it won't be any different for the IRS deal-

ing with a state. They will have access to your activities in Nevada.

When I speak, I have people come up to me that lay out these elaborate schemes that involve trusts and Nevada corporations. I am told that they are perfectly protected from all creditors and that they don't have to pay any income taxes to the IRS. There is no such possibility. I always look at them and envision how they will look in stripes. Nevada has sometimes been oversold – almost like an off-shore tax haven, but it's not that simple.

People always tell me they are going to incorporate in Nevada and then move all of their rents and income to the Nevada corporation. Thus, they won't have to pay any state income tax. That's not true. No matter where you are incorporated, if money is earned in a state through rents or other means, then the state where the money is earned will want its state income tax, and they are entitled to it.



If you are not registered in the state where your company owns property or are doing business, the laws of the state will not protect you. For example, if you don't properly register in the state, your tenant can sue the corporation (you) and the courts will simply allow them to take the property if they win. After all, as far as that state is concerned, there isn't any corporation, just a

piece of property in the state. If the corporation wants to evict the tenant, it can't, because the state won't recognize it as an entity that can bring suit.

My bottom line is, in most all cases you should incorporate or form your LLC in the state where the property is or where the company conducts the major part of its business. You will save lots of money by not having a presence in states where you really don't need to have a presence. Recognize that the first priority is to "maintain" your company no matter what state you are doing business in. Nevada will give you a 2-3% better asset protection factor, but in 99% of the cases, your attackers will get to their goals long before they ever face the "extra" protection Nevada offers, because you will have slipped up on your own turf, and they don't ever have to face the Nevada issues. If you are going to go public with your company, then incorporate in Delaware. Otherwise, you can't really give me a good reason to incorporate in a foreign state. ■